

Docket No. 00-0812  
Staff Ex. 2.0

DIRECT TESTIMONY  
OF  
JAMES ZOLNIEREK

TELECOMMUNICATIONS DIVISION  
ILLINOIS COMMERCE COMMISSION

DOCKET NO. 00-0812

**PUBLIC VERSION**

October 25, 2005

1 **Q. Please state your name and business address.**

2 A. My name is James Zolnierек and my business address is 527 East Capitol  
3 Avenue, Springfield, Illinois 62701.

4

5 **Q. By whom are you employed and in what capacity?**

6 A. I am employed by the Illinois Commerce Commission as Interim Manager of the  
7 Policy Department of the Telecommunications Division.

8

9 **Q. Please state your education background and previous job responsibilities.**

10 A. I earned my Doctor of Philosophy degree in economics from Michigan State  
11 University in 1996. Prior to joining the Illinois Commerce Commission I was  
12 employed by the Federal Communications Commission ("FCC") in the Common  
13 Carrier Bureau, Industry Analysis Division.

14

15 **Q. What is the purpose of your testimony in this proceeding?**

16 A. The purpose of my testimony is to address wholesale discounts that apply when  
17 Verizon North Inc. and Verizon South Inc. (collectively, "Verizon") resell their  
18 retail telecommunications services in Illinois to carriers pursuant to section  
19 251(c)(4) of the Telecommunications Act of 1996 ("1996 Act").

20

21 **Section I: Recommendation**

22

23 **Q. What wholesale discount rate do you recommend the Commission approve**  
24 **in this proceeding?**

25 A. I recommend the Commission approve a uniform wholesale discount rate of  
26 14.5% that will apply when Verizon resells its retail telecommunications services  
27 in Illinois to carriers pursuant to section 251(c)(4) of the Telecommunications Act  
28 of 1996 (“1996 Act”).

29

## 30 **Section II: Background**

31

32 **Q. What wholesale discount rate did Verizon propose in its initial testimony in**  
33 **this phase (Phase II) of the proceeding?**

34 A. Verizon proposed a wholesale discount rate of 11.40% in circumstances when  
35 the reseller uses Verizon’s OS/DA functions and 13.11% in circumstances when  
36 the reseller does not use Verizon’s OS/DA functions.<sup>1</sup>

37

38 **Q. How did Verizon derive these figures?**

39 A. At a high level Verizon derived its proposed wholesale discount by summing the  
40 retail revenues it earned from selling services that are subject to the resale  
41 requirements of section 251(c)(4) of the Telecommunications Act of 1996 (“1996  
42 Act”), identifying the costs it avoids when provisioning these services, and then  
43 calculating avoided costs as a percentage of retail revenues.

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<sup>1</sup> See Direct Testimony of Verizon witness Joseph S. Williams, Verizon Ex. 2. 0 (“Williams Direct”), at 3.

45 **Q. Have Verizon and Staff agreed upon an appropriate discount rate in this**  
46 **proceeding?**

47 A. Yes. After Verizon submitted its initial testimony in this phase of the proceeding,  
48 Staff and Verizon engaged in talks aimed at identifying and settling any disputes  
49 regarding the appropriate discount rate for wholesale services. As a result of  
50 these talks, Staff and Verizon agreed that a uniform wholesale discount rate of  
51 14.5% is appropriate when Verizon resells its retail telecommunications services  
52 in Illinois to carriers pursuant to section 251(c)(4) of the Telecommunications Act  
53 of 1996 (“1996 Act”).

54

55

56 **Section III: Wholesale Discount Derivation**

57

58 **Q. What is the basis for your recommendation that the Commission approve a**  
59 **discount rate of 14.5%?**

60 A. I agree with Mr. Williams that the methodology described above and used by  
61 Verizon to derive the wholesale discount proposed in his Direct Testimony is, as  
62 a general matter, consistent with relevant determinations of Eighth Circuit Court  
63 of Appeals and the Federal Communications Commission’s Wireline Competition  
64 Bureau.<sup>2</sup> However, Verizon’s actual implementation of this methodology fails to  
65 conform, in one respect, with this Commission’s guidance on computing  
66 appropriate wholesale discount rates. In Docket No. 95-0458/95-0531 (Consol.)  
67 the Commission stated that “...in removing the avoided retail costs in reaching a

68 wholesale discount rate, a pro-rata share of contribution pertaining to avoided  
69 retail functions must also be removed.”<sup>3</sup> Verizon did not make this adjustment in  
70 calculating the figures it submitted in its initial testimony in this phase of the  
71 proceeding.

72

73 **Q. What is the result of making such an adjustment?**

74 A. Using publicly available information, in conjunction with information submitted by  
75 Verizon, I estimate that making this adjustment will produce a discount rate of  
76 14.45%. I calculated this figure as follows:

77

78 First, I calculated an estimate of the Verizon return for products and services  
79 subject to resale. According to information reported by Verizon to the FCC,<sup>4</sup>  
80 Verizon had total 2003 intrastate operating revenues of \$346,466,000.  
81 According to information reported by Verizon to the FCC,<sup>5</sup> Verizon had total 2003  
82 intrastate operating expenses of \$273,350,000. Assuming revenues and  
83 expenses for products and services subject to resale are incurred in proportions  
84 comparable to total revenues and expenses, an estimate of the return on  
85 expenses for products and services subject to resale equals (total intrastate  
86 operating revenue – total intrastate operating expenses)/(total intrastate  
87 operating expenses) or  $(\$346,466,000 - \$273,350,000) / \$273,350,000 = 26.7\%$ .

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<sup>2</sup> See Williams Direct at 4-5.

<sup>3</sup> Commission Order in Docket No. 95-0458/95-0531 (Consol.) at 18.

<sup>4</sup> Total Operating Revenues from Verizon’s cumulative (for COSAs “COIL”, “GLIL”, and “GTIL”) 2003 ARMIS 43-01 Row “1090”, Column “Y2003 State (g)” for Illinois.

89 Second, I calculated the pro-rata share of the contribution pertaining to avoided  
90 retail functions. This figure equals (the estimated return on expenses for  
91 products and services subject to resale)\*(avoided retail expenses excluding a  
92 pro-rate share of contribution pertaining to avoided retail functions<sup>6</sup>) or \*\*\*BEGIN  
93 CONF XXXXXXXXXXXXXXXXXXXXXXXXXXXX END CONF\*\*\*.

94  
95 Finally, I calculated the wholesale discount on products and services subject to  
96 resale. Total avoided costs for products and services subject to resale equals  
97 (avoided costs for products and services subject to resale excluding a pro-rata  
98 share of contribution pertaining to avoided costs for products and services  
99 subject to resale) + (the pro-rate share of contribution pertaining to avoided costs  
100 for products and services subject to resale) = \*\*\*BEGIN CONF  
101 XXXXXXXXXXXXXXXXXXXXXXXXXXXX END CONF\*\*\*. The wholesale percentage discount  
102 on products and services subject to resale, therefore, equals (total avoided costs  
103 for products and services subject to resale)/(retail revenues from products and  
104 services subject to resale<sup>7</sup>)\*100= \*\*\*BEGIN CONF  
105 XXXXXXXXXXXXXXXXXXXXXXXXXXXX END CONF\*\*\*.

106  
107 **Q. Has Verizon agreed to a proposed wholesale discount rate that is**  
108 **consistent with removal of a pro-rata share of contribution pertaining to**  
109 **avoided retail functions?**

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<sup>5</sup> Total Operating Expenses from Verizon's cumulative (for COSAs "COIL", "GLIL", and "GTIL")  
2003 ARMIS 43-01 Row "1090", Column "Y2003 State (g)" for Illinois.

<sup>6</sup> Williams Direct, Ex. JW-1, Page 2 of 15, Line 21 + Line 23, Column entitled "Avoided Amount."

<sup>7</sup> Williams Direct, Ex. JW-1, Page 2 of 15, Line 11, Column entitled "Regulated Intrastate Amount."

110 A. Yes. As noted by Verizon witness Phillip J. Wood, Verizon has agreed to accept  
111 a discount of 14.5%.<sup>8</sup> Thus, Verizon has accepted a figure that, in my opinion,  
112 reasonably adjusts Verizon's figures to remove a pro-rata share of contribution  
113 pertaining to avoided retail functions.

114

115 **Q. Have you identified any further adjustments that should be made to**  
116 **Verizon's proposed wholesale discount rate?**

117 A. No. I have not identified any evidence that indicates further adjustments should  
118 be made.

119

120 **Q. Does this conclude your testimony?**

121 A. Yes.

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<sup>8</sup> See Direct Testimony of Verizon witness Phillip J. Wood, Jr. ("Wood Direct") at 13.